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February 8, 1993

92-266

Office of the Secretary
Federal Communications Commission
1919 M Street, N. W.
Washington, D. C. 20554

Dear Sirs:

The enclosed is submitted pursuant to the Federal Communications Commission's request for comments in the matter of Notice of Proposed Rulemaking, MM Docket No. 92-266 pertaining to cable television Rate Regulation. The original and nine copies are enclosed.

Please do not hesitate to contact me at the above address and telephone number if additional information is needed to properly evaluate the enclosed comments.

Sincerely,

Ronald B. Mallard
Cable Television
Administrator/Director

Enclosures

Before the

FEDERAL COMMUNICATIONS COMMISSION

Washington, D.C.

In the Matter of	)	
	)	
Implementation of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket No. 92-266
	)	
Rate Regulation	)	

REPLY COMMENTS OF FAIRFAX COUNTY, VIRGINIA

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REPLY COMMENTS OF FAIRFAX COUNTY, VIRGINIA

I. INTRODUCTION

On October 5, 1992, the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act" or "Act") was enacted by the United States Congress. In passing the 1992 Cable Act, Congress directed the Federal Communications Commission ("FCC" or "Commission") to establish rules and regulations to implement the Act's provisions. In its Notice of Proposed Rule Making ("NPRM") released on December 24, 1992, the FCC seeks comment on the adoption of policies and procedures relating to the regulation of rates for cable service.

The 1992 Cable Act allows local government authorities to regulate basic cable rates, installation charges, and rates for equipment provided by the cable company consistent with the rules adopted by the Commission in this proceeding. The Act further states that the FCC will regulate the provision of cable programming services (exclusive of premium and pay-per-view channels) on higher (expanded) tiers. Congress found that rate regulation has become necessary since cable rates have consistently risen each year substantially more than inflation.

Consumer dissatisfaction with such increases is clearly evident in the number of complaints received by the County since cable rates began increasing immediately after Federal rate deregulation occurred in December 1986. During this period, rate complaints has been one of our highest categories of cable consumer complaints, most recently averaging around 19% (i.e. 165) of the total number of complaints the County received in 1991-1992. The high rate of increase in cable service charges to County citizens since December 1986 has caused these complaints. Since that time, for example, basic or "Limited" service has risen 354% for a majority of County subscribers. Expanded basic or "Full" service has risen 155%. Both levels of increase far outpaced the rate of inflation during this period (i.e. cumulatively 27%). Accordingly, cable television subscribers in the County will be directly and immediately affected by the rate regulation rules adopted by the FCC in this proceeding if such rules act to return rates to a more reasonable level.

By way of background, two cable television systems currently are franchised to serve the residents of the three franchise areas in Fairfax County. The two largest franchise areas, encompassing approximately 300,000 homes, are served by Media General Cable of Fairfax, Inc. ("Media General" or "MGC"). MGC's subscriber system currently comprises over 3,850 plant-miles with over 200,000 subscribers (including those in the separately franchised cities and towns). It is a dual cable, 450 MHz system with an 126 channel capacity. Over 90 of these channels are active currently.

From 1983, when the first subscriber was connected to MGC's system, through 1986, Media General offered three tiers of basic service and several premium channels. Rates were frozen during this period in accordance with the terms of the franchise agreement and Section 623 of the Cable Communications Policy Act of 1984 ("1984 Cable Act"). Initially, the monthly charge for Tier I, which contained 39 channels, was $3.07; for Tier II, which contained 53 channels, the monthly charge was $9.36; and for Tier III, which contained 61 channels, there was a monthly charge of $11.36. The monthly charge for premium services was $7.95 per channel.

In December 1986, federal rate deregulation legislation preempted the County's franchise terms regarding rates, thus allowing the cable companies to raise rates without any limitations. Since then, MGC has raised its basic service rates seven times. Specifically, in 1987, Tier I, which by then contained 43 basic channels, was changed to "Limited Service" and the monthly charge went from $3.07 to $4.95. This charge has now increased to $13.95 per month for 43 channels, which constitutes a 354% increase in seven years for basic service. Tier II, which accounted for approximately two-thirds of all subscribers, was dropped concurrent with the initial rate increase in 1987, and those who previously subscribed to Tier II were required to subscribe to Tier III at a higher cost if they wished to receive their previous level of service.

The charge for Tier III (re-named "Full Service"), which included 74 basic channels in 1987, went from $11.36 to $12.95 per month in that year. The monthly rate for this service has increased every year since then, most recently to $28.95 for 75 channels, effective February 1, 1993. This constitutes an 155% rate increase (209% for previous Tier II customers) in this service cost between 1986 and 1993.

The smaller, separate Reston franchise area of the County is served by Time Warner Cable of Reston ("Time Warner" or

"TW"). Time Warner's subscriber system encompasses over 150 plant-miles of dual, 330 MHz cable. It passes nearly 20,000 homes, including more than 12,700 subscribers and offers an 80 channel capacity. Over 60 of these channels are active currently.

Prior to the passage of the 1984 Cable Act, Time Warner (at that time, known as "Warner Cable Communications of Reston") was unfranchised and unregulated by the County. Pursuant to the provisions of the 1984 Cable Act, TW applied for a County franchise, which was awarded in early 1988. Prior to the time the franchise took effect, TW offered 21 channels of basic service, 7 channels of expanded basic service, and 3 pay channels. The company charged $10.95 per month for its basic service, $17.20 per month for expanded basic and $11.95 per month for each pay channel. In 1989, Time Warner began to offer a single, upgraded Standard basic service with 51 channels at a cost of $17.80 per month. In 1991, TW returned to two levels of basic service with Basic (21 channels) costing $16.75 per month and the higher tier Standard service (50 channels) costing $22.52 per month. In 1992, Basic service remained at $16.75 per month and Standard service was increased to $24.10 per month. During the five year period since the franchise was awarded, this constitutes a 53% increase in the cost of entry level basic service and a 41% increase in expanded basic service.

II. DISCUSSION

The discussion which follows addresses the issues in the NPRM that most significantly and directly affect the citizens of Fairfax County. Each section of the discussion is referenced by the paragraph to which it relates in the NPRM.

1. Paragraph 2 - Objectives of Rate Regulation and Implementation Procedures.

The FCC seeks comment on the type of regulatory model that best fulfills the rate regulation statutory objectives. In its NPRM, the FCC favors a benchmarking approach to basic rate regulation and disfavors the cost-of-service approach. The County agrees that the benchmark approach can be the primary method of initially establishing basic cable service rates. However, in establishing and using such an approach the Commission must address many variables as discussed in the following sections. As further discussed in these comments, the County believes that the cost-of-service approach should remain an alternative for the use of regulatory authorities when it can be shown that the benchmarking approach is not meeting the Congressional objective of arriving at a reasonable and competitive service cost through rate regulation.

2. <u>Paragraph 4 - Reduction in Rates</u>.

The FCC seeks comments on the impact and use of rate reductions should such reductions be justified after applying the guidelines established in these proceedings. The County recommends that all regulated rates which are higher than those calculated to be reasonable under FCC guidelines, be reduced to comply with the guidelines. This is essential if the new FCC regulations are going to address the apparent intent of Congress. The primary reason that the FCC is addressing rate regulation is that Congress believes that existing basic rates are too high and that increases in such rates over the last several years have been unreasonable when compared to inflation.

Several industry observers have stated that an alternative to rate reductions could be the implementation of rate freezes. These observers believe that leaving existing rates in place over a period of years will eventually allow today's service costs to be deemed reasonable in a future year, at which time rate increases would be allowed again. The County disagrees because this approach would not counteract the effect of excessive monies paid by consumers in past years and it would leave inordinately high prices in effect for years to come. Therefore, any unreasonable current rates must promptly be reduced to a level determined to be reasonable under the FCC guidelines.

3. Paragraph 8 - Standard for When Households are Considered to be Offered Competitive Video Programming Services.

The FCC seeks comment on what standard should be applied in determining when households are offered competitive video programming in the determination of effective competition. The County believes that such competitive services should only be considered "offered" to households if they are effectively and demonstrably marketed to potential subscribers. Also, the County recommends that other multichannel services only be considered as "competitive" to cable services if they provide a substantial number of the same channels as those offered on the existing cable system's tiers.

4. Paragraph 9 - Definition of a Multichannel Video Programming Distributor.

The FCC seeks general comment on what providers qualify as "multichannel video programming distributors" for purposes of determining effective competition. The FCC also seeks specific comment on whether a video dialtone (VDT) provider qualifies as a multichannel video programming distributor. Generally, the County recommends that any multichannel video provider that offers services that meet the definitions of either basic cable service or cable programming service should be considered competitors to those services under the FCC's tests for effective competition. However, following on the County's recommendation in the previous section, the FCC must also define some categories and numbers of programming that must be present on competitors' expanded tiers in order for the services offered by different providers to be considered comparable.

In regard to video dialtone, the County believes that, subject to the conditions described above, some VDT providers may be within the definition of a multichannel video programming distributor. However, as the County has stated in previous proceedings, VDT competitors would not be operating on a "level playing field" with cable systems because video dialtone providers need not be locally franchised under the FCC's current rules. Such a condition amounts to unfair competition from the view of a locally-franchised cable operator. It also will foster unfair comparisons between the two enterprises and regulatory structures. Again, as stated previously, the most effective way to remedy this problem is to allow local franchising of VDT outlets.

5. <u>Paragraph 17 - Finding of Effective Competition</u>.

The FCC seeks comment on whether the local franchising authority should be responsible for showing that effective competition does not exist before exercising its rate regulation authority. The County strongly recommends that the FCC establish in these proceedings a presumption that effective competition does not exist in any jurisdiction, unless the cable operator demonstrates otherwise. Placing this burden on franchising authorities will cause local governments to unnecessarily expend time and resources when current national statistics indicate that there is little, if any, multichannel competition anywhere in the U. S. Further, it is likely that franchising authorities would be subject to frequent requests by cable operators to demonstrate the absence of effective competition and frequent challenges when such an absence is reported. Consequently, requiring local authorities to prove a lack of effective competition would add unnecessarily to the costs of regulation and create an increased potential for undue litigation. To avoid these problems, the burden should be placed on the regulated entity, the cable operator, who has the incentive to continuously monitor and prove the existence of competition.

6. Paragraph 32 - Programming on the Basic Tier.

The FCC seeks comment on the extent to which these regulations should emphasize the creation of the lowest possible priced basic service tier and the extent to which rate regulations should affect the cable operator's basic tier programming and pricing flexibility. The County believes that the affordability and availability of basic cable service should be a primary goal of the FCC in crafting regulations in this proceeding. Achieving this goal would seem to mandate that operators create basic tiers that contain only the Congressionally-required minimum offering (broadcast and Public, Educational and Governmental, or PEG, access channels). However, in developing programming on their basic service tiers to meet community needs, cable operators may have to take into account several factors, such as market demographics, costs of programming, penetration levels, and subscriber desires, that will serve to expand their basic offerings beyond the minimum required. The County believes that the FCC can allow flexibility in the number and types of channels placed on the basic tier to meet community needs, as long as the tier continues to comply with the definition of basic cable service and does not conflict with the primary goal of developing a reasonably priced service.

7. Paragraph 33 - Benchmarking and Cost-Based Rate Regulation.

The FCC seeks comment on their conclusion that a benchmarking method of setting basic service rates should be the primary mode of regulating basic service rates. The FCC further concludes that cost-of-service regulatory principles can be applied in a secondary role if benchmark regulation is not appropriate in a particular situation. The County agrees in principle with this approach to basic rate regulation, subject to two important conditions. First, a benchmark formula, that allows for local customization of a number of variables, should be developed in lieu of a national benchmark rate. Second, cost-of-service regulation should only be employed as an alternative at the sole discretion of the franchising authority. These conditions are discussed further in the next few sections.

8. Paragraphs 34, 37, 49, and 53-56 - Benchmarking.

The FCC seeks comment on how to implement a benchmark approach to basic rate regulation. Essentially, the County recommends the use of a benchmark formula, with locally customized variables, in lieu of a national benchmark rate. While any benchmark approach will avoid some of the problems of cost-of-service based pricing, the County believes that only a benchmark formula, that allows consideration of a number of factors quantified at the local level, will establish a benchmark that can be applied fairly and equitably in each individual cable television service area.

The County recommends that such a benchmark formula begin with the direct costs of signals provided on the basic tier, plus a reasonable mark-up to recover a nominal percentage of joint and common costs between all tiers. The primary component of direct costs would be programming expenditures for the number and types of channels on the basic tier. This component would include, for example, any broadcast channel retransmission consent costs. Also calculated into this component would be the mitigating effect of any revenue-generating channels, such as classified ad, promotional and home shopping channels. All programming costs would be tested for reasonableness based on national averages for similar services in competitive markets. Initially, if competitive data is not available because of a lack of competitive markets, the lowest priced cost for similar services could be used as the basic test for the reasonableness of any given system's programming costs.

Once a rate figure has been calculated based on direct cost plus a nominal contribution to joint and common costs, it can then be subjected to a number of locally quantified variables. These variables should include, but not be limited to, a market area cost-of-living factor and a construction and operating efficiency factor. The cost-of-living variable will allow the basic formula to be adjusted to account for higher service delivery costs in a specific locale. The efficiency factor will allow modification of the basic formula to counteract company inefficiencies. This will ensure that the undue cost of inefficient operation is absorbed by the company and not passed on to the subscriber. Other local variables may also be pertinent to include in the benchmark formula. The FCC should allow local franchising authorities to add such variables as needed, if it can be shown that they are crucial in determining a reasonable rate.

National benchmarking, which would not allow proper consideration of these and other costs at the local level, may actually provide certain disincentives. For example, some systems will not explore ways to operate more efficiently if a widely applicable benchmark is used for those systems that is so high as to allow profits to continue even in the face of inefficient operation. Additionally, benchmark rates that do not allow for consideration of such factors could end up being very attractive to one cable system while being detrimental to another system, even though the systems may be similarly sized and operate in the same geographical area.

Therefore, the County recommends that if a benchmark approach is adopted by the FCC, that it be formulaic, flexible and allow for customization by the local regulatory authority based on the factors listed above. Franchising authorities would then be able to use the benchmark formula to establish a basic rate that reflects efficient operation, proper cost allocation and provision of a useful, affordable basic offering by the local cable operator.

9. Paragraph 38 - Inflation Each Year.

The FCC seeks comment on how a benchmark should be adjusted for inflation each year after it has initially been established in these proceedings. The County recommends that any automatic increase in the benchmark established for any cable system be no more than the local Consumer Price Index (CPI) experienced for the previous year. Such an increase will not only be more understandable by and acceptable to subscribers, it will allow cable operators to benefit from their own cost saving initiatives should their costs not increase by the CPI in any given year.

10. Paragraph 47 - Current National Average Rates Used as a Benchmark.

The FCC seeks comment on the validity of defining benchmark rates based on current average industry rates. The County views this approach as unacceptable since the current level of basic rates is considered to be unreasonable and is based on monopolistic market power. These industry rates are the principal factor that propelled the enactment of the 1992 Cable Act's rate regulation provisions. Any regulatory scheme based on current average industry rates would be unreasonable and contrary to Congressional intent.

11. Paragraphs 57-61 - Cost-of-Service Based Rate Regulation.

The FCC seeks comment on the advantages and disadvantages of cost-of-service regulation. The County agrees with the Commission that this method should not be the primary method of regulating basic rates. However, it should remain a secondary alternative to be utilized by the franchising authority as needed, if the calculated benchmark rate is deemed unreasonable. Many factors will have to be addressed under the cost-of-service method of rate regulation, such as rate-of-return, depreciation methods, cross subsidies within cable systems and between other corporate subsidiaries, etc., that could severely burden the regulatory authority if it was the primary method of rate regulation.

12. Paragraph 66 - Charges for Equipment.

The FCC seeks comment on the methodology to be used in the establishment of price regulation for equipment (i.e., converters, remote control units, etc.). The County agrees that it would be reasonable to establish prices for equipment that would recover the direct costs of such equipment plus a nominal percentage markup for indirect costs. The County also recommends that the FCC ensure that the subscriber has a choice to use the cable operator's equipment or buy such equipment from other vendors on the open market. Such subscriber choice could remedy a problem that the County and other jurisdictions have experienced regarding the inability of subscribers to directly interface their own consumer electronic devices (televisions, VCRs, remote controls, etc.) with the cable system without substantial cost or technical difficulties.

13. Paragraphs 69-71 - Installation Charges.

The FCC seeks comment on the appropriate methodology to determine charges for installation. First, the County believes that the franchising authority should be empowered to approve or disapprove all charges for installation before they become effective. Second, the franchising authority should be able to review installation charges using an average cost-based methodology that considers the service drop distances involved, home wiring that is currently in place, affordability of installation for low-income households and other pertinent factors. With this information, the franchising authority will be able to determine standard, average installation costs that are fair and reasonable.

14. Paragraphs 73 and 175 - Franchising Costs on Customers' Bills.

The FCC solicits comment on the proper interpretation of the 1992 Cable Act's provisions that certain amounts can be shown separately on subscribers' bills that are attributable to franchise requirements. The County believes that Congress intended for franchise costs itemized on bills to only include those verified costs directly attributable to PEG access funding and equipment requirements, and franchise fees. Other franchise requirements were not considered by Congress for itemization and should not be listed separately on subscribers' bills. Specific costs that should not be itemized include the normal costs of doing business for any service and those franchise requirement costs that benefit the business in total. For example, the costs of an operator's customer service operation should not be itemized as a franchise requirement, regardless of what customer service standards are included in the franchise. Customer service is a normal business function for a service company. Additionally, efficient customer service will drive revenue for the operator. The franchising authority also should review and approve such itemized costs prior to their appearance on subscribers' bills.

15. Paragraphs 80-87 - Local Franchising Authority's Review Period for Basic Tier Rates.

The FCC seeks comment on the amount of time the franchising authority should be given to review and approve or deny a requested change in basic service rates. In reviewing any rate increase request, the regulatory authority will want to provide formal notice to the public of such a proposed change in rates and provide an opportunity for public comment on concerns about cable service and the requested rate increase. The County believes that this could require a period of up to 180 days from the time a regulatory authority receives notice of a rate increase request to the time a final decision on the rate increase is made by the regulatory authority. This 180 day period is consistent with the timeframe specified by the Cable Communications Policy Act of 1984.

16. Paragraphs 100 and 102 - Subscriber Complaints Concerning Expanded Tier Rates.

The FCC seeks comment on what approach should be adopted for the filing and review of subscriber complaints to the Commission on expanded basic rates. The FCC also seeks comment on how their review should be coordinated with a local franchising authority. The County believes that this process should be kept simple. If the subscriber believes the rates are unreasonable, they should file a complaint in writing to the FCC, the local regulatory authority and the cable operator. The Commission should then seek input from both the franchising authority and the operator before taking final action on the complaint.

17. Paragraph 124 - Information to be Provided by Cable Operators.

The FCC seeks comment on the appropriate scope of information that it should collect from cable operators for the purposes of rate regulation. Based on past difficulties in obtaining necessary financial information, the County recommends that the FCC establish comprehensive minimum requirements for information to be provided by cable operators to regulatory authorities. Further, local authorities should be allowed to require additional information as needed to properly evaluate current and proposed rates. If the requested information is readily available, then the cable operator should be required to respond to the franchising authority within 10 days. If the information is not readily available, then the cable operator should be required to respond in a reasonable time, such as 30-60 days. The County agrees with the Commission that it would be appropriate for the FCC to collect the information described in Appendix C to this NPRM from every cable system in order to facilitate proper rate regulation. Such information should be easily accessible to the franchising authority. Additionally, a uniform accounting system, such as that described by the FCC in Appendix A to the NPRM, should be established and followed by all cable operators. This will allow effective cost comparisons to be made between systems, ensure the reasonableness and accuracy of the records maintained by the cable operator and facilitate efficient, effective and defensible rate regulation.

III. CONCLUSION

The County's comments in this proceeding pertain to those issues in the NPRM that most directly affect cable subscribers. Additionally, the County finds much support for its comments in other testimony filed in this proceeding. Based on this, the County's major recommendations are as follows:

- Any basic service rates currently in effect, that are determined to be unreasonable under the Commission's rules established in this proceeding, must be promptly reduced to reasonable levels.

- o In defining the existence of effective competition, the FCC should only include those multichannel video program distributors that have effectively and demonstrably marketed their service to households and offer a substantial number and mix of the same channels as those offered on the existing cable system's regulated tiers.

- o The FCC should adopt a rule in these proceedings that there will be a presumption that effective competition does not exist in any jurisdiction, unless the cable operator demonstrates otherwise.

- o The FCC should establish a benchmark formula as the primary method of regulating basic rates. The formula should allow local regulatory authorities to customize the benchmark based on consideration of various factors so that the resulting benchmark rate is equitable and encourages efficient operations. The locally customized benchmark can then be adjusted for inflation each year based on the Consumer Price Index.

- o As a secondary approach, when the benchmark rate is found to be unreasonable, a cost of service approach to basic rate regulation may be used at the sole discretion of the franchising authority.

- A benchmark rate must not be established based on the average cable industry monopolistic prices currently charged to subscribers.

- The FCC should establish pricing formulas for subscriber equipment that would recover the direct costs of such equipment plus a nominal percentage markup for indirect costs. The FCC should ensure that subscribers have the choice to use the cable operator's equipment or buy such equipment from independent vendors.

- The FCC should adopt a methodology for establishing installation charges that is average cost-based and the local franchising authority should approve any such installation charges before they become effective.

- Only the costs of itemized, franchise requirements directly identifiable and verifiable as PEG access funding and equipment and franchise fees can be shown on subscribers' bills. The franchising authority should review and approve such itemizations prior to their appearance on the bills.

- In order to provide for formal notice to the public of proposed rate changes and provide an opportunity for public comment on such changes, the FCC should allow franchising authorities 180 days to rule on a requested rate adjustment.